Five ways smart companies maintain growth and profitability.

PART II

The economy is relatively healthy, but history has taught us that growth cycles don't last forever. Knowing that there's a cyclical pattern to many markets, savvy owners and executives figure out how to take advantage of business cycles to create a continuing growth trajectory and boost profitability. In last month's newsletter, we looked at the first two action items that are critical to middle-market companies for maximizing growth, profitability, and value in any economy, including:

1. Develop a strategic plan

2. Grow your customer base

This month, we will be diving into action items 3 and 4. Let's take a look.

3. Make better decisions through data analytics

Many middle-market executives are concerned they're behind the trend when it comes to data analytics. Indeed, it holds great potential for improving decision making and thereby performance, profitability, and value. We also see a lot of hype around data analytics, making it easy to jump in without a deliberate and flexible approach.

Data analytics is the transformation of information into actionable insights that can lead to competitive advantage. There are three types.

- Descriptive analytics answers questions such as, "What happened and why?" "Why is turnover so high?" "How much does it cost, or how long does it take, to hire a new employee?"
- Predictive analytics takes that a step into the future, answering "What will happen if...?" Amazon's product recommendations are a great example of how predictive analytics can be used to suggest other items you might like based on your history, wish list, and other customer purchases.
- Prescriptive analytics go another step further, pointing to specific actions to take depending on the outcome you seek. Google Maps is a good example. Enter your destination and, based on your current location, traffic, network of available roads, and previous preferences, Google displays what it thinks is your optimal route.

All three types of analytics lessen the personal biases and preferences we so often use to make decisions. As good as our instincts may be, analytics reduce uncertainty. They also can lead to improved efficiency and revenue. Companies use analytics to experiment with real-time pricing based on demand, inventory, and data about how much different customers will pay. Manufacturers use data analytics for preventive maintenance to reduce downtime and prevent shortages. Others use it for insight into absenteeism patterns to predict plant shifts that may be short-handed. And one property and casualty client that had sat on years of archived adjustor reports turned data into $12 million in subrogation recoveries.

You might think analytics is the province of large corporations, but...not so. Smaller companies may have the advantage here. The trove of data middle-market companies possess likely will be easier to mine. Still, you must be intentional. Data is an asset, and organizations that get that are culturally well-positioned to leverage it.

Align questions with business strategy

We often use the analogy of a house when we talk about data analytics, and your business strategy functions as the all-important roof. Any project or initiative must fit under that roof — that is, align with your strategy. This ensures the questions you ask, and the answers you uncover, contribute directly to gaining competitive advantage or solving a particular problem.

The walls of the metaphorical house represent performance management. What are your key performance indicators (KPIs)? When making the investment in a data analytics program, you need a systematic way of measuring progress against your business objectives.

Organizational infrastructure — people and processes — are the support beams of the house. This is by far the greatest challenge for many businesses. The results of your data analytics projects will drive change in how people work. Spreadsheets and old processes go away, and this can make people uncomfortable. Strong leadership commitment and involvement are key to smoothing transitions.

The cost of undertaking data analytics initiatives is often a concern, but the investment doesn't have to be prohibitive. How much to invest should be based on the type of business. Certainly, if you're Uber, and your business model relies on analytics to deliver services, then yes, you'll have to spend more. Otherwise, many reasonably priced tools with robust capabilities exist today. In addition to software costs, you should plan to spend up to five times that amount for services and labor to normalize data.

Narrow the focus to start

We recommend companies begin with a pilot. Focus on one aspect of the business and identify specific questions to answer. To find that fitting first project, look at your internal and external stakeholders — shareholders, customers, staff, suppliers, and others. Develop a plan for what information you'll retrieve to answer the question and how you'll apply the results. The pilot you conduct should be important to a key constituency and enable you to move the needle on KPIs, in alignment with your strategy.

Formalize your program by involving the right people, including leadership. Your IT folks and many other functional areas should be involved but not leading the charge. Data analytics is not "an IT thing." Create a sandbox, make mistakes, learn, and then widen the scope to tackle more.

4. Take a flexible approach to real estate

The space a business occupies does a lot: It can enhance your brand and company image, attract talent, support growth, and help drive and maintain profitability. Does your office space attract and retain staff? Here are a few things to consider as you evaluate your real estate in the months and years to come.

Think about space needs early

Last-minute decisions can be costly. Our clients know we're not kidding when we counsel them to start thinking about their next move the day after they sign a lease. Planning ahead for company growth and expansion is especially important now since space is limited. Pickup has been slow after the last two recoveries. There isn't a lot of new construction, and we don't expect that to change in the near future.

While long-range planning is critical, long-term promises can be expensive

We can all think of companies who, in 2008, lost significant business and found themselves with too much space on their hands and too much time left on their lease. Negotiate termination and contraction clauses carefully up front, and seek expert input to be sure you understand the full impact. There are costs associated with termination and contraction, but at least you know what they'll be and can plan ahead.

Be creative — and consider millennials' open office needs

Look at how your business currently uses its space and the styles your employees need to work in. Sometimes staff need to be heads down and focused; sometimes they need to be more collaborative. Does your space accommodate these varied seating arrangements? Just as you build flexibility into your lease agreements, you want to build flexibility into the space itself.

Benchmark against your peers to learn how they configure their space. Bring HR into the decision-making process, and look at the demographics of your staff and at larger trends. Be creative — hoteling, desk sharing, multiple seating configurations for solitary and collaborative work. Any number of options exist, with plenty of upside potential.

Over 50 percent of the workforce is composed of millennials, and remote work arrangements are still rising. We had one client with a traditional office build-out and significant employee turnover. Each employee move cost $3,600. The company spent more on internal moves than rent! By reconfiguring the space into an open office design, we were able to drop the client's cost to $30 per move.

It's a new era for lease accounting

New Financial Accounting Standards Board (FASB) guidance will have far-reaching implications for how leases are reflected on your company financial statements. The most significant change is that lessees will be required to report lease obligations on their balance sheet, with few exceptions.

Especially if you have historically structured lease arrangements as operating leases, you may see significant lease obligations on your financial statements. This change could impact operating and financing decisions, thereby requiring you to reevaluate your "brick & mortar" and debt-sourcing strategies going forward.

Review your existing leases. Make sure you and your accounting and finance team understand all the implications around the recording of assets and liabilities, buy vs. lease decisions, sale-leaseback arrangements, related party leases, financing decisions, and other considerations to ensure your financial statement and real estate strategies are in alignment. Then make appropriate changes to internal IT systems and controls, and clearly communicate the changes and impact to stakeholders.

Changes went into effect December 2018 for public companies and go into effect December 2019 for private firms.

Next month we'll take a look at action item 5 and conclude this three-part series.

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